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LONG RUN STOCK PERFORMANCE OF MALAYSIAN ACQUIRERS

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Introduction

Mergers and acquisitions (M&A) is one of the largest forms of corporate investment (Masulis, Wang & Xei, 2007). Acquisitions, especially the large ones, have long term consequences on the well-being of shareholder and other stakeholders as they are risky in nature. Existing studies provide substantial evidence on poor performance following completion of merger deals (see for example Aggrawal and Jaffe, 2000 for an extensive literature review). Most of the evidence on mergers in the context of developed countries document that for long-run stock performance, the average abnormal returns for bidding firms are at best zero return (Martynova & Renneboog, 2008). This result shows that M&As do not add value to the bidding firms. In this study, we focus on Malaysia, a developing economy where many firms are controlled by families. The sample is composed of acquisitions during the period 2000-2013. We find that on average acquiring firms neither create nor destroy long term values after controlling for the performance of a control group. This result shows that investors reacted rationally in valuing the bidding firms after the announcements of the completions of the acquisitions. Thus, at least in the long run performance of acquisitions, the capital market in Malaysia is informationally efficient.

Problem Statement

The long run performance of stock returns has been a debatable issue. Some studies attribute the performance of long-run stock returns to the misvaluation of a firm's securities. For example, when bidders use overvalued shares to finance acquisitions, this would lead to the underperformance of stock returns for the acquiring firms (Ma, Whidbee & Zhang, 2011; Ang & Cheng, 2006). Several other studies attributes long-run stock performance by forwarding extrapolation hypothesis (Rau and Vermaelen, 1998; Lin, Chou & Cheng, 2011). They argue that investor and management overestimate the bidders' past performance. Another explanation of long-run stock performance is highlighted by Fama (1970, 1998), Andrade, Mitchell and Stafford (2001), and Dutta and Jog (2009). They contend that long run stock performance is affected by market efficiency. A market is efficient if security prices reflect available information (Fama, 1970). The idea of efficient market has received considerable attention from researchers. For instance, Andrade, Mitchell and Stafford (2001) claim that due to an efficiency with respect to public information, stock prices quickly adjust following a merger announcement, incorporating any expected value changes. Their

study shows zero returns. Similarly, Dutta and Jog (2009) claim that their insignificant findings in long-term abnormal returns is consistent with the market efficiency hypothesis. Their arguments stem from the fact that anomalies are chance results, where overreaction of stock prices to information is as common as under-reaction. Therefore, post-event continuation of pre-event abnormal returns is frequent as post-event reversal.

Literature Review

In this section, an overview of the existing literature on long run stock performance using different benchmark and approaches is provided. There are mixed evidence on studies of long run returns to bidding firms. King, Dalton, Daily and Covin (2004) carry out a meta-analysis of 103 studies and find that long-run returns, range from six months to three years, to bidding firms are negative and statistically significant at 1%. They argue that the results imply that acquisitions do not lead to synergistic benefits to bidders. Ma, Whidbee and Zhang (2011), Chu Lin, Kai Chou and Chi Cheng (2011), Moeller, Schlingemann and Stulz (2005), and Andrade, Mitchell and Stafford (2001) find that acquisitions in the US lead to wealth destruction to bidders. However, when value-weighted approach is used, Andrade, Mitchell and Stafford (2001) find that acquisitions do not influence long run performance. Nevertheless, the evidence from China (Bhabra & Huang, 2013; Jing, Qian & Martin, 2011) and India (Banerjee, Banerjee, De, Jindra & Mukhopadhyay, 2014) show that acquisitions lead to better long run performance. A recent study by Bougarrou and Navatte (2013) find that family's bidder in France outperform than non-family's bidder. Given various explanation forwarded to explain long run performance, current studies has yet reach a consensus. The dispute is partly due to different benchmarks used and approaches in estimating abnormal returns. In Malaysian market, the puzzle of long-run stock performance of acquisition is still under explored. Thus, this study attempts to provide an explanation for long run share price performance.

Sample Selection and Methodology

The sample is composed of completed acquisitions between 2000 and 2013. Two return metrics are used: cumulative average abnormal returns (CAARs) and buy and hold abnormal returns (BHAR). To examine the abnormal returns, the returns to bidding firms are adjusted by using returns of two benchmarks: market portfolio, which is proxied by FBM EMAS Index, and a portfolio of matching firms (Barber & Lyon, 1997). Matching firms are identified based on market value (MV) and market-to-book value (MTBV). Data on firm size (MV), market-to-book value (MTBV) and stock prices are taken from Thompson DataStream.

Long-term Stock Performance Measurement

To measure long-term stock performance, we use an event study methodology as recommended by Barber and Lyon (1997) and Khotari and Warner (1997). We estimate thirty-six month abnormal performance as cumulative average abnormal returns (CAARs), beginning from the month following the completion of acquisition. This study also employ another method to compute abnormal returns which is buy and hold abnormal returns (BHAR), following Barber and Lyon (1997) and Lyon, Barber and Tsai(1999).

Two benchmarks for price performance are applied (a) the market benchmark approach using FBM Emas Index and (b) matching firm. Following recommendations of Barber and Lyon (1997) and Lyon, Barber, and Tsai (1999) abnormal returns are estimated using a control firm as a benchmark, selected according to two criterias: size and market to book ratios. To choose control firms, Euclidean distance approach is used.

To ensure a good matching between sample firm and matching firms, three portfolio of matching firms are used, which is made up of one-firm, two-firms and four firms. Average market value (MV) and market to book value (MTBV) of bidding firms is RM626.569 million (1.121) while the average MV (MTBV) of the portfolio of matching firms is RM638.261 million (1.059), RM602.105 million (1.055) and RM586.810 million (1.030) for one-firm, two-firm and four-firm respectively. The differences between the market values and market-to-book values of the portfolios of matching firms and those of bidding firms are not statistically significant at a 10%-level.

Analysis and Discussion

Results for long run performance using CAAR and BHAR are reported accordingly in Table 1 and Table 2. In Table 1, the result of the cumulative average raw returns of the bidding firms over a three-year period following acquisitions is summarized. Column 1a of Panel A shows that the equal-weighted (EW) raw returns to bidding firms are positive and increasing. In the first year following acquisitions, bidding firms earn an average return of 4.976% and it increases to 21.438% over a three-year period. However, the positive result might be driven by good market performance.

To investigate if the results are due to acquisitions, the raw returns have to be compared against the returns of a benchmark. Columns 2a to 5a summarize the performance of the bidding firms after adjusting for the performance of a benchmark by using EW-CAAR. When the performance of the bidding firms is adjusted for the performance of a benchmark, none of the results is significant. These results show that acquisitions do not lead to over-or under-performance of the bidding firms. In fact, investors react rationally to acquisition completions and their expectations of the future performance do not differ from the actual future performance. In this case, the market, at least in term of the long-run performance of acquisitions, is efficient in Malaysia. When value-weighted (VW) measures are used as reported in Panel B of Table 1, the results are basically similar to the equal-weighted results. Again, these results show that investors form an unbiased expectation of the future performance.

Table 1: Raw returns and cumulative average abnormal returns (CAAR) to bidding firms

MONTH	NO. FIRMS	Cumulative average abnormal raw return (1a)	CAAR KLSE Adj (2a)	CAAR -ONE MATCH (3a)	CAAR- TWO MATCH (4a)	CAAR - FOUR MATCH (5a)
Panel A (Equally-Weighted)						
1 to 12	267	4.976% ^a (0.067)	-3.570% (0.121)	-2.705% (0.327)	-2.710% (0.304)	-4.218% ^a (0.084)
1 to 18	266	10.409% ^c (0.004)	-1.860% (0.567)	-2.086% (0.623)	-3.301% (0.365)	-3.686% (0.283)
1 to 24	261	11.863% ^c (0.008)	-4.379% (0.294)	-3.148% (0.531)	-3.925% (0.374)	-4.279% (0.312)
1 to 30	257	17.811% ^c (0.000)	-3.767% (0.414)	-1.570% (0.780)	-3.713% (0.446)	-4.447% (0.347)
1 to 36	252	21.438% ^c (0.000)	-5.638% (0.236)	-1.991% (0.737)	-4.957% (0.346)	-6.425% (0.203)
Panel B (Value Weighted)						
1 to 12	267	4.742% (0.587)	-0.957% (0.896)	3.327% (0.678)	-0.891% (0.897)	-2.489% (0.752)
1 to 18	266	1.037% (0.930)	-7.499% (0.412)	-1.049% (0.920)	-4.683% (0.592)	-7.238% (0.472)
1 to 24	261	5.350% (0.602)	-6.931% (0.397)	0.611% (0.950)	-4.312% (0.545)	-4.100% (0.628)
1 to 30	257	16.654% ^c (0.001)	0.127% (0.977)	8.123% (0.115)	3.789% (0.508)	4.172% (0.305)

a,b and c indicate 10%, 5% and 1% respectively

Table 2 summarizes the results using buy-and-hold returns. Column 1a shows that the equal-weighted (EW) raw buy-and-hold returns to bidding firms are positive. In the first year following acquisitions, bidding firms earn an average return of 5.538% and it increases to 10.827% over a three-year period. When EW buy-and-hold compared to those of the benchmarks, we find that the BHAR are negative if KLSE (-17.528%), two-firm portfolio (-10.309%) or four-firm portfolio (-10.667%) is used as the benchmark. These results show that there is an evidence of under-performance or over-reaction by investors when EW measure is used. However when VW measure is used, none of the BHAR is significant except when KLSE is used as the benchmark, where the BHAR is -6.898% and significant at 10%. The insignificance of BHAR when VW approach is used shows that the underperformance of EW-BHAR is driven by small firms. Overall, the results of buy-and-hold returns reflect those of cumulative average returns especially when VW measures are used.

Table 2: Raw returns and buy-and-hold abnormal returns (BHAR) to bidding firms

MONTH	NO. FIRMS	Cumulative buy-and-hold raw return (1a)	BHAR KLSE Adj (2a)	BHAR -ONE MATCH (3a)	BHAR- TWO MATCH (4a)	BHAR - FOUR MATCH (5a)
Panel A (Equally-Weighted)						
1 to 12	267	5.538% ^a (0.076)	-3.652% (0.181)	0.105% (0.975)	-0.812% (0.788)	-2.363% (0.373)
1 to 18	266	8.479% ^b (0.031)	-4.528% (0.202)	-0.076% (0.987)	-2.800% (0.495)	-3.028% (0.414)
1 to 24	261	7.694% ^a (0.068)	-9.074% ^b (0.019)	-2.579% (0.614)	-3.929% (0.383)	-3.960% (0.328)
1 to 30	257	11.571% ^b (0.017)	-10.262% ^b (0.027)	-1.183% (0.844)	-3.921% (0.448)	-4.105% (0.379)
1 to 36	252	10.827% ^b (0.020)	-17.528% ^c (0.000)	-4.861% (0.451)	-10.309% ^a (0.091)	-10.667% ^b (0.034)
Panel B (Value Weighted)						
1 to 12	267	7.024% (0.414)	0.766% (0.914)	5.426% (0.469)	1.600% (0.804)	-0.419% (0.954)
1 to 18	266	6.852% (0.530)	-2.476% (0.762)	4.803% (0.595)	0.533% (0.945)	-1.568% (0.856)
1 to 24	261	6.202% (0.519)	-6.493% (0.389)	0.311% (0.970)	-2.667% (0.703)	-3.685% (0.624)
1 to 30	257	16.415% ^b (0.018)	-2.128% (0.663)	8.028% (0.159)	1.974% (0.791)	3.598% (0.473)
1 to 36	252	16.274% ^c (0.005)	-6.898% ^c (0.094)	4.916% (0.465)	0.735% (0.925)	1.398% (0.790)

a,b and c indicate 10%, 5% and 1% respectively

Conclusion

This paper examines the long run stock performance of acquirer companies. Using sample of 208 Malaysian acquisitions during 2000 to 2013, we find that Malaysian market is efficient as stock over performance is hardly observed over the long run. This suggests that our market is efficient as investors' expectation for future performance is similar to the future performance. The findings have implication to trading strategies. While investors can make profit out of Mergers and acquisition announcement, over the long run, traders could ignore the purchase of acquirers' shares as it does not give profit to the stock's traders.

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